



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

SMALL BUSINESS/SELF-EMPLOYED DIVISION

August 21, 2006

SB/SE Control #: SBSE-25-0806-033
Expiration Date: August 21, 2007
Impacted IRM: 25.1

MEMORANDUM FOR SBSE EXAMINATION AREA DIRECTORS, TERRITORY
MANAGERS, GROUP MANAGERS AND SPECIALTY
PROGRAMS CHIEFS

FROM: Eileen C. Mayer/s/ [Eileen C. Mayer](#)
Director, Fraud/Bank Secrecy Act

K. Steven Burgess/s/ [Monica L. Baker \(for\)](#)
Director, Examination

Bill Conlon/s/ [Bill Conlon](#)
Director, Specialty Programs

SUBJECT: Timely Actions in the Development of Fraud Cases

The purpose of this memorandum is to emphasize the importance of continuing to take timely actions on potential civil and criminal fraud cases. Although cases in Status Codes 17 and 18 are exempt from overage measures (IRM 25.1.2.1(6)), timely actions are still important, especially in the development of fraud. The most successful cases have been those where the examiner, with the support of the group manager, take timely and appropriate actions in case development. The number of cases in status 17, fraud development status, has increased significantly in recent months. Many of these cases include multiple years and have been open for prolonged periods of time. It is important that we emphasize the need for taking appropriate action.

For your convenience, below you will find some pertinent Fraud Handbook IRM guidance for recognizing and developing fraud cases:

- IRM 25.1.2.1(2) recommends that the examiner initiate a discussion with their group manager and the local Fraud Technical Advisor (FTA) when the first indications of fraud are uncovered. A plan of action should be developed jointly as early as possible to document the affirmative acts of fraud. An integral part of the plan is establishing that sufficient affirmative acts exist to confirm fraud. The plan should be a joint effort of the examiner, the group manager and the FTA.

The action plan will help guide the case to its appropriate conclusion in a timely manner. It is important to note that the role of the FTA can be more than advisory or consultative. The jointly developed action plan can and should specify any direct assistance the FTA will provide. The action plan should be retained in the work papers. It should be noted that some cases may not require a face to face meeting with the FTA. While consultations over the phone or email are possible, face to face contact is preferable.

- IRM 25.1.2.1(6) states that when it is agreed by the examiner, the group manager and the FTA that potential for fraud exists, the case will be updated to Status Code 17 (Fraud Development Status). The Form 11661 is used to document the FTA's involvement and to document the decision to update the case to Status Code 17. Cases should be returned to Status Code 12 if it is determined that the potential for fraud does not exist. However, cases should not be placed into or out of Status Code 17 without consulting the FTA. The reasons and the decision to return a case to Status Code 12 should be documented on the Form 11661. If a disagreement exists on whether a case should or should not be in a fraud development status, the ultimate decision rests with the group manager.
- The examiner, with assistance from the FTA, must know when to suspend action on a case and prepare a criminal referral when there is a firm indication of fraud. If the examiner stops too soon, all information necessary to document firm indicators (affirmative acts) of fraud may not be developed sufficiently for Criminal Investigation (CI). IRM 25.1.2.1(8) advises that the examiner or group manager should not obtain advice and/or direction from CI for a specific case under examination. The FTA is available for this consultation. If a criminal referral is not warranted, the FTA can assist the examiner to ensure the civil fraud penalty is properly considered and developed.

The lack of original returns in case files often adds significant time to the development of fraud cases. Effective immediately, all case years that are part of a criminal referral must include original tax returns. Civil fraud penalty cases should also contain original returns. Examiners should request the original returns, if not in the case file, when cases are placed in fraud development status (Status Code 17) for every year that has fraud potential including related returns. IRM 25.1 will be updated to incorporate this requirement.

An operational review template has been created for Territory Managers (TM's) as a guide for use during the review of a group's fraud program and cases. See the attached file. This template can assist TM's in addressing the timeliness of fraud cases, pointing out opportunities for improvement and help identify best practices that may serve as tools for others.

If you have any additional questions, you or a member of your management staff may contact Peggy LeBar, Senior Fraud Program Analyst in Fraud/BSA, at (859) 669-5006.

Attachment

Fraud Analysis Tool
Territory Manager Operation Review

Review	Comments
General Actions	
Ensure via 4502 reviews and workload reviews that the group manager is sufficiently involved in the employees inventory so as to know when a potential criminal/civil fraud case is in process	
Inquire as to the last time the local FTA was in the group for a meeting or presentation to discuss fraud investigations and procedures. Would the group or manager benefit from some additional training? FTA managers will assist.	
Review ERCS for project codes and source codes that are conducive to fraud, follow up as to those started and un-started cases	
Ensure cases that have a potential understatement of income of \$10,000 or more are being discussed with the manager, and the FTA is being consulted where warranted. Consider ATAT, OCC, High Income Non Filer, etc	
EQMS – consider standards 3 and 4-E, is the income probe accurate and appropriate, is fraud being considered	
STATUS 17	
<p>Obtain an extract ERCS report in advance of the review and discuss the cases in status 17 with examiners and the manager</p> <ul style="list-style-type: none"> • How long has the case been in status 17? • Is the action plan being followed ? • Has the FTA been contacted to discuss significant developments? 	

Fraud Analysis Tool
Territory Manager Operation Review

<ul style="list-style-type: none"> • Are timely actions being taken per the action plan? • Are all appropriate tax periods being controlled and in status 17? 	
<p>Compare the status 17 report with the inactive case time report</p> <ul style="list-style-type: none"> • Are status 17 cases being worked as priorities? 	
<p>Compare the status 17 report with the overage inventory report</p> <ul style="list-style-type: none"> • Are timely actions being taken? 	
<p>Consult with the FTA manager in advance of the review</p> <ul style="list-style-type: none"> • Are all cases for which an 11661 form been prepared still in status 17? • If not, was the change to status 12 appropriate? • If referred to CI – see below. • What is the FTA, and the FTA G/M's overall observation relative to the fraud climate in the group? 	
STATUS 18	Comments
<p>Consult with the FTA manager in advance of the review to ensure 100% accuracy in group ERCS records and the fraud database</p>	
<p>Review minutes of 4 way quarterly meetings for all joint investigations -</p> <ul style="list-style-type: none"> • Is the investigation proceeding ratably? • Is the examiner's commitment reasonable as to time and activity? • Are all civil statute's addressed? • Are all years appropriately controlled on ERCS? 	

Fraud Analysis Tool
Territory Manager Operation Review

Has the FTA manager been consulted on any/all cases where there is a potential for CI to discontinue the criminal case?	
CIVIL FRAUD	Comments
Has the FTA been part of the decision to recommend and pursue civil fraud?	
Has the manager or the agent decided to not pursue civil fraud after FTA involvement? IMPORTANT – needs to be discussed with FTA manager to ensure accuracy of fraud database.	
Is the penalty fully developed, and is an alternative position included?	
OTHER CONSIDERATIONS	Comments
Review the Fraud Handbook, IRM 25.1.1 et al	
Is the group demonstrating effective use of the Income Probe and Fraud Development lead sheets?	